

# SUMMARY ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Oller Analyst: Marion Mann DeJong Bill Number: SB 220

Related Bills: See Prior Analysis Telephone: 845-6979 Amended Date: 04/16/2001

Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Backup Generator and Related Hook-Up Switching Equipment Credit

DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended \_\_\_\_\_.

AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

☒ AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced February 14, 2001.

☒ FURTHER AMENDMENTS NECESSARY.

DEPARTMENT POSITION CHANGED TO \_\_\_\_\_.

☒ REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED February 14, 2001, STILL APPLIES.

OTHER - See comments below.

## SUMMARY

This bill would create a tax credit for the purchase of a generator and related equipment used to produce emergency electricity.

This bill also would amend the Health and Safety Code to allow the use of generators during a stage 1, 2, or 3 emergency energy alert. These changes do not affect the department and are not discussed in this analysis.

## SUMMARY OF AMENDMENT

The April 16, 2001, amendments specify that the Franchise Tax Board and not the State Air Resources Board (ARB) would administer the tax credit and that the ARB would determine if equipment qualified for the credit. The April 16, 2001, amendments also made changes to the Health and Safety Code provisions of the bill that do not impact the credit provisions.

Except for the implementation concerns regarding the ARB's administration of the tax credit and certification of the equipment, the department's analysis of the bill as introduced still applies. The "Position," "This Bill," "Implementation Concerns," and "Arguments/Policy Concerns" from the prior analysis have been updated to reflect the amendments and are provided below for your convenience. Amendments are needed to resolve the implementation concerns. Department staff is available to assist the author with any amendments.

Board Position:

<input type="checkbox"/> S	<input type="checkbox"/> NA	<input type="checkbox"/> NP
<input type="checkbox"/> SA	<input type="checkbox"/> O	<input type="checkbox"/> NAR
<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input checked="" type="checkbox"/> PENDING

Legislative Director

Date

Brian Putler

06/12/01

## **POSITION**

Pending.

## **ANALYSIS**

### THIS BILL

This bill would create a tax credit equal to 100% of the cost paid or incurred during the tax year for the purchase of a backup generator and related hook-up and switching equipment. The bill directs the Franchise Tax Board to administer this credit.

A “backup generator” would be defined by Section 41511.3 of the Health and Safety Code to mean an electrical generator operated for the purpose of providing emergency power to a customer that otherwise purchases power from a utility.

The taxpayer would not be allowed to claim any deductions, including the business expense or depreciation deductions, for any cost of the generator or related equipment for which the credit is allowed.

Personal Income Tax (PIT) taxpayers could carry forward any unused credit for a maximum of five years. Bank and Corporation (B&C) taxpayers could carry forward any unused credit indefinitely.

### IMPLEMENTATION CONCERNS

The department has identified the implementation concerns listed below. Department staff is available to work with the author’s office to resolve these and other concerns that may be identified.

- The term “related hook-up and switching equipment” is not defined. Undefined terms can lead to disputes between taxpayers and the department.
- The definition of “backup generator” seems to be inconsistent with the understood purpose of this bill. The purpose of the credit is to provide an incentive for taxpayers to purchase generators and related equipment to produce their own electricity during an energy emergency. The credit would be allowed for the purchase of a “backup generator,” which is defined as a generator operated to provide emergency power to a customer that otherwise purchases power from a utility. Despite the understood purpose of this bill, the present language could be interpreted to permit the credit for a generator that produces electricity for a person other than the taxpayer claiming the credit.
- Taxpayers and department staff do not have independent expertise in the area of generators and related equipment and thus may have difficulty determining if the equipment qualifies for the credit. Having independent expert verification of the property would help the department in administering this credit. Although the author amended the bill with the intent to have ARB determine if equipment qualifies for the credit, the bill does not specify what the ARB is to “determine.”
- The carryover period for unused credit for PIT taxpayers is different than it is for B&C taxpayers. This may cause taxpayer confusion, especially for shareholders in S corporations. The S corporation could carry forward the unused credit indefinitely while the shareholder could carry forward any unused credit for a maximum of five years. This issue can be resolved by making the carryover periods consistent.

## **ARGUMENTS/POLICY CONCERNS**

This bill does not limit the credit exclusively to generators or related equipment that are used or installed in California.

The bill implies, but does not require, that a generator be used during a power emergency. The Health and Safety Code provisions of the bill are related to generators used for emergency power during a stage 1, 2, or 3 emergency energy alert. However, the credit is allowed for the purchase of any generator regardless of when or if the generator is used. Other than possible air violations enforced by the State Air Resources Board, the language would permit taxpayers to use the generator at any time. On the other hand, if the credit were restricted to generators used only during a stage 1, 2, or 3 emergency energy alert it would be difficult to determine when generators were actually used. In addition it could be difficult for taxpayers and department staff to determine that a generator was used on a stage 1, 2, or 3 emergency energy alert during an audit conducted a few years after use.

This bill does not specify a repeal date or limit the number of years for the carryover for B&C taxpayers. Credits typically are enacted with a repeal date to allow the Legislature to review their effectiveness. However, even if a repeal date were added, the department would be required to retain the B&C carryover on the tax forms indefinitely because an unlimited credit carryover period is allowed. Recent credits have been enacted with a carryover period limitation since experience shows credits are typically used within eight years of being earned.

The bill does not provide for the recapture of the credit if the generator or related equipment is sold or no longer used within a specified time, or simply removed from the state. Moreover, since the credit is granted at the time the costs to purchase are paid or incurred, it is theoretically possible for taxpayers to resell these generators among themselves to generate multiple credits. That is because there is no mechanism to require actual use for a specified time.

Conflicting tax policies come into play whenever a credit is provided for an item that is already deductible as a business expense or is depreciable. This credit would require an adjustment to reduce basis to eliminate the double benefit of receiving both the credit and the expense deduction or depreciation deduction. However, this adjustment would create a basis difference for state and federal purposes, which is contrary to the state's general conformity policy.

Credits generally are provided as a percentage of amounts paid or incurred. This bill would allow a 100% credit, which is unprecedented.

## **LEGISLATIVE STAFF CONTACT**

Marion Mann DeJong  
Franchise Tax Board  
845-6979

Brian Putler  
Franchise Tax Board  
845-6333